12

Integrating CSR into the Corporate Governance Framework: The Current State of Indian Law and Signposts for the Way Ahead

Richa Gautam

1. Introduction

Traditionally, the role of the corporate[1] was clear—with its roots in agency principles, a corporate's responsibility lay towards its principals. Its only responsibility towards stakeholders other than its principals was what society had established through various environmental, labour, and other societal-protection legislations. In today's world however, corporates (for reasons ranging from the business case to philanthropic considerations) are recognising a responsibility to stakeholders that goes beyond their legal responsibilities. As corporates increasingly recognise and act upon this corporate social responsibility (CSR), policy-makers are also searching for innovative ways in which corporates can contribute to a country's sustainable development agenda. One such example is the incentive structure of CSR credits mooted in 2010 by Salman Khurshid, India's Minister of Corporate Affairs.[2]

This paper seeks to examine the nature of CSR in India, and the legal framework best suited for the integration of certain aspects of CSR into corporate policies and practices, and also seeks to explore how corporates and policy-makers can (in light of existing laws) integrate certain elements of CSR into the legal framework of corporate governance.

2. Defining corporate social responsibility

An issue that has prevented CSR from attaining the status of a concrete discipline is the fact that definitions of CSR[3] abound and remain somewhat agenda-driven, shaped by the context and objectives of those defining it. While concepts such as the Triple Bottom Line (Elkington, 1997), and CSR standards that set forth indicators of economic, social, and environmental criteria of operations have gained popularity, no single definition has gained universal acceptance. Too often CSR is defined for the purposes of a specific organisation, country, or group of stakeholders (e.g. investors) in terms of mission statements, or CSR standards, or other voluntary instruments.

International CSR standards and instruments seek to identify the boundaries of what constitutes CSR. The United Nations' Global Compact is a classic example; the details of the ten principles are given in Box 1. Another is the draft of the ISO 26000 Standard on Social Responsibility of the International Organization for Standardization (ISO), which is among the most comprehensive documents to set the contours of a corporate's responsibility towards a range of stakeholders including the environment, labour, consumers, and the community.[4]

Box 1: Ten principles of the UN Global Compact

Human Rights
- Principle 1: Businesses should support and respect the protection of internationally proclaimed human rights; and
- Principle 2: make sure that they are not complicit in human rights abuses.

Labour Standards
- Principle 3: Businesses should uphold the freedom of association and the effective recognition of the right to collective bargaining;
- Principle 4: the elimination of all forms of forced and compulsory labour;
- Principle 5: the effective abolition of child labour; and
- Principle 6: the elimination of discrimination in respect of employment and occupation.

Environment
- Principle 7: Businesses should support a precautionary approach to environmental challenges;
- Principle 8: undertake initiatives to promote greater environmental responsibility; and
- Principle 9: encourage the development and diffusion of environmentally friendly technologies.

Anti-Corruption
- Principle 10: Businesses should work against corruption in all its forms, including extortion and bribery.

Source: http://www.unglobalcompact.org/AbouttheGC/TheTENPrinciples/index.html (Accessed on 18 August, 2010).

A parallel discourse is that of business and human rights, a key framework for which has recently been developed by John Ruggie, the United Nations Special Representative to the Secretary General, which establishes the three-fold duty of "protect, respect and remedy".[5]

A key question in examining the legal framework for CSR is whether compliance with laws is part of CSR, or whether CSR starts where the law leaves off. Although traditionally CSR has been defined as "beyond law", in a country like India with a poor record of enforcement of environmental and labour laws, there is value in including legal responsibilities as the lowest rung within the framework of a corporate's responsibilities (Gautam, 2010).[6] In other words, compliance with the law is a necessary minimum, although it should not be the entire extent of a corporate's responsibility.

While the CSR discussions in the West have largely focused on businesses reducing their negative impacts (or improving their positive effects) on people and the planet, the Indian CSR discussion emphasises another element—philanthropy. Arguing that philanthropy has been a part of business, especially the ubiquitous family businesses in India through the ages, Sundar (2000; cited in Sood & Arora, 2006) traces the history of corporate philanthropy from the second half of the nineteenth century. The emphasis on philanthropy is also reflected in the practice of Indian corporates and their sponsored foundations,[7] especially in areas like health, education, and poverty alleviation, to such an extent that the term CSR is often used synonymously with philanthropic or community development initiatives.

The significance of corporate philanthropy, in addition to environmental, social and ethical responsibility, has also been highlighted in Indian CSR instruments, ranging from the Indian Prime Minister Manmohan Singh's Ten-point Social Charter for corporates,[8] to the voluntary codes developed by the Confederation of Indian Industry (CII) and the Federation of Indian Chambers of Commerce, as well as the Voluntary CSR Guidelines issued by the Ministry of Corporate Affairs (MCA) (highlights of the Voluntary CSR Guidelines are provided in Box 2).

In this paper, the term corporate social responsibility (CSR) is used to connote the responsibility of a corporate—including but extending beyond its legal responsibility—towards the environment and society, determined through its engagement with its stakeholders, and which encompasses the minimising of its adverse impact on stakeholders, as well as its contribution to their sustainable development through philanthropic initiatives.

Box 2: Framework of the Voluntary CSR Guidelines, Ministry of Corporate Affairs, India

Fundamental Principle
Each business entity should formulate a CSR policy to guide its strategic planning and provide a roadmap for its CSR initiatives, which should be an integral part of overall business policy and aligned with its business goals. The policy should be framed with the participation of various level executives and should be approved by the Board.

Core Elements:
The CSR Policy should normally cover [the] following core elements:

1. Care for all Stakeholders
2. Ethical functioning
3. Respect for Workers' Rights and Welfare
4. Respect for Human Rights
5. Respect for Environment
6. Activities for Social and Inclusive Development

Implementation Guidance:
In addition, the MCA Voluntary CSR Guidelines provide implementation guidance, including allocation of a specific amount in the budget for CSR activities and structured dissemination information on their CSR.

Source: http://www.mca.gov.in/Ministry/latestnews/CSR_Voluntary_Guidelines_24dec2009.pdf (Accessed on 18 August, 2010).

Should a corporate owe a responsibility beyond legal compliance?

There are of course those who argue that a corporate should not owe a responsibility beyond legal compliance. Many point to the Friedmanite assertion that the only social responsibility of business is making money.[9] However the proponents and practitioners of CSR give several reasons why a corporate should think beyond its legal obligations. These drivers range from ethical considerations among business leaders, to long-term sustainability of the corporate, which is a major concern for certain investors.[10] Value to the corporate itself (i.e. business case for CSR) is one of the more popular drivers in terms of reduced risks or costs, or improved performance.

Several case studies have attempted to identify the environmental, social, or governance factors that lead to improved financial or operational performance, as for instance, in the matrix in Table 1 (SustainAbility and International Finance Corporation, 2002, available at www.sustainability.com).

Table 1: Business case matrix

The business case matrix		**Sustainability factors**						
		Governance & engagement		Environmental focus		Socio-economic development		
		Governance & management	Stakeholder engagement	Environmental process improvement	Environmental products and services	Local economic growth	Community development	Human resource management
Business success factors	Revenue growth & market access							
	Cost savings & productivity							
	Access to capital							
	Risk management & license to operate							
	Human capital							
	Brand value & reputation							

Source: SustainAbility and International Finance Corporation (2002).

From the more obvious factors like "brand value and reputation" to the more esoteric factors like "social license to operate" (i.e. acceptance from the community within which the corporate operates), corporates across sectors, geographies, and levels of maturity see different reasons that make the business case for CSR (Association for Stimulating Know

How, 2010; Global Reporting Initiative, 2009; SustainAbility and International Finance Corporation, 2002; SustainAbility and UNEP, 2001; among others).

Once CSR is defined and it is accepted that corporates can and should have a responsibility that goes beyond merely compliance with laws, the next question is how a corporate should go about addressing these responsibilities.

Appropriate framework to address CSR responsibilities

Being a cross-cutting issue, different aspects of CSR fall under different functions within a company, and this becomes problematic when addressing the CSR responsibilities of the company as a whole. Environmental matters are looked into by a different department from the one that looks into anti-corruption, while yet another one looks into project-related displacement of communities—there is generally no single body or structure tasked with examining the impact of corporate policies across stakeholders. Therefore it is suggested that the only way to address a cross-cutting issue like CSR is to bring CSR within a cross-cutting (or rather, overarching) regime that is well-established within corporates—the corporate governance framework.

Within the corporate governance framework, there are several corporate governance institutions and structures into which social and environmental concerns can usefully be integrated.[11] Two such institutions that have the potential to impact all other aspects of corporate governance are the responsibilities of the board of directors, which cover oversight of all corporate functions; and the reporting and disclosure regime, which again is geared towards collecting and processing financial and select non-financial information from different functions within the organisation.

Having defined CSR to not only include but also go beyond compliance with the law, both of these areas of contiguity are discussed below in terms of what Indian law currently provides for, and suggestions are made for how CSR can be effectively integrated into the corporate governance framework (drawing on the experience of other countries as well as examples from other fields of law within India).

3. Responsibilities of the board of directors towards stakeholders

Although there is a rich body of case law in India on the duties of individual directors (mostly negative duties against insider trading, making personal profit off a corporate opportunity, etc.), the legal framework does not clearly lay down the role of the board as a whole.[12] Even less guidance exists on the role of the board as regards stakeholders other than shareholders, although the Kumar Mangalam Birla Committee sought to achieve this by balancing the claims of stakeholders and shareholders. The Kumar Mangalam Birla Committee Report (1999) identified the fundamental objective of corporate governance as the "enhancement of shareholder value, keeping in view the interests of other stakeholders," seeking to harmonise "the need to enhance shareholders' wealth whilst not in any way being detrimental to the interests of the other stakeholders in the company" (para 4.2). However such a systemic approach regarding the board's obligations towards the stakeholders has not yet found its way into the corporate governance legal framework.

In other words even the limited duties towards stakeholders that are imposed under corporate law are implemented in a scattered way. Very few corporates have a cohesive approach to identify and engage with their stakeholders.

Board responsibilities to stakeholders: Current state of Indian law

The legal framework for corporate governance in India consists by and large of the Companies Act, 1956 which applies to all companies (and is expected to be replaced in 2010 with a new Companies Bill), and Clause 49 of the Equity Listing Agreement that binds listed companies. Under the law relating to corporate governance, the Board is required to consider the interests of various stakeholders in specific contexts (some of which have been collated in Box 3). In addition the provisions of several environmental and social legislations also come into play, especially as relates to directors' responsibilities and liability.

Box 3: Current state of Indian corporate law on responsibilities of the board to stakeholders

Stakeholder	Legal duty of the board to consider the interests of such stakeholder
Employees	Right to be heard in case of significant proceedings involving the company such as schemes of arrangement or winding up of the company. Responding to a workers' petition to be heard in the winding up of a company, the Supreme Court of India has held that "the company is a species of social organization, with a life and dynamics of its own and exercising a significant power in contemporary society. The new concept of corporate responsibility transcending the limited traditional views about the relationship between management and shareholders and embracing within its scope much wider groups affected by the trading activities and other connected operations of companies, emerged as an important feature of contemporary thought on the role of the corporation in modern society".[40] Information to be placed before the board under the Listing Agreement specifically includes matters impacting labour, such as fatal or serious accidents, dangerous occurrences, and significant labour problems and their proposed solutions, significant developments on Human Resources/Industrial Relations front like signing a wage agreement, implementation of Voluntary Retirement Scheme, etc.[41]
Environment	Although approached from an energy savings point of view, Section 217(1)(e) of the Companies Act requires the board report to discuss energy conservation measures of the company in the previous year (see Box 4 for details). Material effluent or pollution problems are required to be placed before the board under Annexure IA to Clause 49 of the Listing Agreement.
Consumers	Annexure IA to Clause 49 of the Listing Agreement also requires the board to be informed about any issue which involves possible public or product liability claims of a substantial nature, including any judgement or order which may have passed strictures on the conduct of the company or taken an adverse view regarding another enterprise that can have negative implications on the company.
Society	The catch-all agenda item of "non-compliance with any regulatory, statutory or listing requirements" under Annexure 1A would bring within the ambit of the board's discussion any non-compliance with the several labour welfare and environment legislations, as well as legislations prescribing a standard of conduct towards sections of society.

Source: Compiled by author, primarily from the Companies Act (1956), and the Listing Agreement.

Additionally businesses are required to comply with several environmental and social legislation,[13] many of which contain an “Offence by Companies” provision which imposes liability on the company as well as “persons in charge of and responsible to the company” for the conduct of its business (subject to due diligence defences). In addition such provisions provide that where an offence is committed with the “consent or connivance of,” or “is attributable to any neglect on the part of” any director, manager, or any other officer of the company, such a person is also deemed to be guilty of that offence. In other words, a director can be liable under such a provision under the environmental and labour laws if he/she is “in charge of” and is “responsible to” the company for the conduct of its business, which in most cases will include the managing director; or the offence is committed with the “consent or connivance” of the director or is attributable to his/her neglect.[14]

The managing director and members of the board have been held to be prosecutable under a similar provision of the Water (Prevention and Control of Pollution) Act, 1974.[15] Similarly, in the case of wage and social security statutes, several cases have laid down that directors can be liable under the first prong of the above test.[16]

Liability for non-compliance inevitably leads to the conclusion that directors are obliged to and should also as a matter of prudence inform themselves of and actively monitor the company’s compliance with laws that impact two of a company’s key stakeholders—labour and the environment. The existence of such liability provisions should therefore be seen as identifying the non-shareholder stakeholders that legislators consider to be a part of the board’s constituency.

Corporate philanthropy and the board’s responsibility

We have (in light of the practice in India) included corporate philanthropy within the definition of CSR in this paper. As was stated earlier, CSR surveys of Indian corporates reveal the significance of philanthropy, especially in the areas of health, education, and poverty alleviation in the surrounding communities. Current corporate law can also be interpreted as allowing a board to engage in corporate philanthropy as long as it is strategic philanthropy (i.e. it creates a business case). Section 293(1)(e) of the Companies Act allows the board to contribute up to Rs. 50,000 or 5% of the average net profits in the previous three years to *"charitable* and other funds *not directly relating to the business of the company or the welfare of its employees"* (emphasis added) without obtaining shareholder approval.[17] The emphasised text has been drawn upon by one of the leading authorities on Indian corporate law (Justice Chandrachud, 2006) to argue that the board has the power to donate the company's property beyond such limits, if some benefit accrues thereby to the company, i.e. if it is strategic philanthropy (p. 2923).[18]

However a revision of this provision has been sought in Clause 160(1)(e) of the Companies Bill, 2009 to entail the requirement of a special resolution of shareholders for the board to "contribute to charitable and other funds as donation in any financial year, an amount in excess of 5% of its average net profits for the three immediately preceding financial years". The revised provision may need to be further clarified since it can be interpreted in two ways as it stands now: (a) as allowing the board (upon receiving shareholder approval) to contribute up to 5% of the average net profits to *non-strategic* or cheque-book philanthropy; or (b) as allowing the board to contribute *any* amount (without limit) to strategic philanthropy that also meets a business case, requiring shareholder approval only for non-strategic charity.

Where the current law falls short and suggestions for the way forward

In the area of the board's responsibilities towards stakeholders, although the responsibilities of the board to specific stakeholders in *specific* situations are defined (see Box 3 for details), these are scattered over different legislations, the compliance of which is monitored by different departments of the company, and are not holistically viewed through the CSR lens. There is no comprehensive guidance to the Board as to stakeholders *generally*, such as for example under the UK Companies Act which requires company directors to consider several identified stakeholders in their actions, including employees, suppliers, customers, the community, and the environment.[19]

This can potentially be addressed at a policy level by the proposed introduction in the Companies Bill (2009) of a specific board committee to consider and resolve the grievances of stakeholders. If passed in its current form, the Companies Bill will require this Stakeholders Relationship Committee to be constituted by all companies with more than 1,000 share-, debenture-, and other security-holders, and to be chaired by a non-executive director.[20] If broadened beyond merely stakeholder grievances, this legislative change can be utilised by corporates as an opportunity to develop a comprehensive strategy to identify stakeholders, engage with them, minimise negative effects on stakeholders in their immediate vicinity and direct corporate philanthropy strategically in a way that benefits key stakeholders.[21]

A reworded Clause 160(1)(e) of the Companies Bill, clarifying the limits (if any) on strategic and non-strategic corporate philanthropy should also fall within the mandate of this Stakeholder Relationship Committee in order to allocate discretionary CSR spending (or philanthropy) among stakeholders in a strategic manner.

4. Disclosure and reporting

The regime relating to disclosure and reporting is one of the cornerstones of corporate governance; the key corporate governance institutions—auditors, audit committee, annual general meeting, etc.—can be seen as various stages of the process of collecting, verifying (auditing), and presenting annual financial information to shareholders in the form of the Annual Report.[22] Although largely limited to financial reporting, some non-financial or CSR data is being reported by corporate India.

The term *CSR reporting* is used here to include reporting on non-financial or environmental, social and governance (ESG) risks and opportunities of the company (also known as ESG reporting or non-financial reporting), as well as reporting on its philanthropic activities.

In India, the term CSR reporting is often limited to the latter, but it clearly needs to embrace the former as well.

CSR reporting fulfils two policy purposes—increased transparency and therefore more effective engagement with stakeholders on CSR issues; and the highlighting of certain environmental and social concerns to the board and management (through the process of collecting material information, and creation of the report by the board and management).

The logic behind reporting to investors on environmental and social risks is unimpeachable. As was shown in the earlier discussion on the business case, there are several ways in which a corporate's social and environmental behaviour can affect its bottom line. In gaining a holistic perspective about a company, why would investors not want to know about potential material environmental and social risks and opportunities that can affect their investment as much as legal and regulatory risks?[23]

Despite the clear value to investors, most countries in the world show a poor record in terms of requiring a *holistic* integration of non-financial items of disclosure into Annual Reports, although *select* non-financial data (especially those which carry a large regulatory price-tag for non-compliance) are often required to be disclosed; e.g. environmental proceedings in the US Form 10-K Annual Report.[24] Similarly Indian law also requires select non-financial criteria to be reported, but as with board responsibilities to stakeholders, this is limited and scattered, having been introduced at different times based on what the current priorities were at that point in time.

CSR reporting: Current state of Indian law

Indian law requires a discussion of select ESG matters in the Annual Report (the significant provisions have been collated in Box 4). There is no such requirement as to disclosure of philanthropic initiatives, although the MCA's Voluntary CSR Guidelines recommend a broader dissemination of "information on CSR policy, activities and progress in a structured manner to all their stakeholders and the public at large through their website, annual reports, and other communication media" (p. 13).

The practice in this case goes far beyond the legal requirement. Several Indian companies voluntarily include ESG disclosure as well as information on their philanthropic programmes and initiatives within their Annual Reports, and some also produce annual Sustainability Reports.[25] However both these groups consist primarily of large corporates. The level or quality of ESG disclosure has also been questioned,[26] as has the general accessibility of this information,[27] unless disclosed on the corporate website. Where one of the aims of CSR reporting is to provide access to the corporate's CSR information to the stakeholders, and thereby improve the quality of stakeholder engagement, the lack of a centralised database where all company filings can be easily accessed by the public poses a serious issue.

Box 4: Current state of Indian law on ESG disclosure in the Annual Report

Subject	Indian law regarding ESG disclosure in the Annual Report
Environment	Section 217(1)(e) of the Companies Act requires the board to report on energy conservation measures by the company in the previous year. Under this Section, the Companies (Disclosure of Particulars in the Report of Board of Directors) Rules (1988) require the Board to report on: (a) the energy conservation measures taken; (b) additional investments and proposals, if any, being implemented for reduction of consumption of energy; (c) impact of the measures at (a) and (b) above for reduction of energy consumption and consequent impact on the cost of production of goods; and (d) total energy consumption and energy consumption per unit of production as per the provided form in respect of certain high energy consumption industries.
Labour	The MD&A report, which is part of the Annual Report, requires discussion of "material developments in Human Resources, Industrial Relations front, including the number of people employed." (Clause 49(IV)(F)(i)(viii) of the Listing Agreement) Quarterly financial results must disclose all events or transactions "material to an understanding of the results for the quarter" which include strikes and lock-outs. (Clause 41(IV)(k) of the Listing Agreement)
Corporate Governance	The Corporate Governance Report should discuss matters such as the company's philosophy on governance, as well as information on various aspects of board, audit committee, related party transactions and non-mandatory good practice matters such as whistle-blower policy and director training.

Source: Compiled by author from the Companies Act (1956), and the Listing Agreement.

The way forward: Two approaches to improved ESG disclosure

In this area it is clear that although small steps are being taken, a holistic overhaul is needed in order to mainstream ESG reporting.[28] This can be done in two ways—through voluntary sustainability reporting, or legislatively, by mandating disclosure of key ESG information within Annual Reports.

Voluntary sustainability reporting: The practice of sustainability reporting is gaining popularity across the world and also in India. Sustainability reporting involves "reporting on economic, environmental, and social impacts",[29] sometimes used synonymously with triple bottom line reporting, corporate responsibility reporting, and non-financial reporting. The most popular framework for sustainability reporting internationally is the Global Reporting Initiative's *G3 Reporting Guidelines*.[30]

Although sustainability reporting provides the most detailed framework for CSR reporting, it is necessarily outside the scope of the legal framework of financial reporting, and provides an alternate (voluntary) framework. Detractors of sustainability reporting also point to the fact that in practice corporates sometimes misuse sustainability reporting for marketing.[31] Since no liability under securities laws attaches to statements made in sustainability reports, unlike those made in Annual Reports,[32] disclosure controls tend to be weaker and such reports therefore sometimes carry statements that are less rigidly vetted than similar statements contained in the Annual Report. On the flip side, mandating significant levels of ESG reporting in the Annual Report is likely to impose burdens on smaller companies, at least in the short run. Therefore, voluntary sustainability reporting by corporates needs to go hand in hand with gradually increasing levels of mandatory reporting of select ESG data in the Annual Report.[33]

Integration of ESG into Annual Reports: Most legal systems (including India) require the disclosure of select ESG criteria in company Annual Reports (see Box 4).[34] Whereas the approaches of most countries are fragmented, some countries have overhauled the disclosure rules to fully integrate ESG factors within the financial reporting framework. The second report of the South African committee on corporate governance, headed by Mervyn King (popularly called the King II report) recommends "integrated sustainability reporting," i.e. an integrated approach to financial and non-financial reporting, including local issues of concern such as HIV/AIDS, and procurement in line with the Black Economic Empowerment Act.

In one of the most comprehensive approaches to mandating non-financial reporting within the Annual Report, the law overhauling the French corporate law in 2001—the *Nouvelles Regulations Economique* (NRE)—introduced a requirement for French listed companies to produce a sustainable development report within their Annual Reports, containing detailed information on human resources, including compensation, health and safety information and gender-diversity data; community involvement, which includes local partnerships with NGOs and others within the community and disclosure of labour compliance by subcontractors; and environment, including resource use, emissions, biodiversity and environmental management.[35]

The sustainable development report is required to be shared with the company's Works Council as well as auditors, and is also to be presented to the board of directors. It therefore is an example of a law that mainstreams CSR concerns within the entire corporate governance structure through CSR reporting. Although initially the quality of reports produced under the NRE was considered poor, there has been a significant increase in focus on CSR within French corporates, which has been linked to the regulatory push factor of NRE.[36]

While the French NRE was the legislative driver to improved ESG reporting, other actors have played a role in this regard in other parts of the world. Self-regulatory organisations (such as stock exchanges) have the mandate as well as the legal flexibility to require companies listed on their exchanges or indices to report on ESG. A case in point is the Malaysian stock exchange (Bursa Malaysia) which began by publishing CSR guidance for companies in September 2006 and gradually worked with Malaysian regulators to move to a mandatory CSR reporting regime. The Malaysian Listing Rules now require Annual Reports of listed companies to include a description of their CSR activities and practices (or to state that there are none).[37]

Regulatory guidance on specific ESG issues: An alternate approach is one that focuses the regulatory push on a specific ESG issue of concern to the country. This is an approach that was successfully followed in the 1988 amendment to the Indian Companies Act that introduced Section 217(1)(e), which requires the Board to annually submit a detailed report on energy conservation measures, including the impact of the measures and the total energy consumption and energy consumption per unit of production. In other words, Section 217(1)(e) requires the boards of certain manufacturing businesses to focus their attention on operational matters such as energy consumption, bringing this otherwise delegated subject to the attention of the highest decision-makers within the corporate.

A recent example on issue-specific disclosure is the interpretive guidance issued by the US Securities and Exchange Commission (SEC) on climate change disclosures. Interpretive guidance does not create legal requirements; it is instead intended to clarify existing requirements. However, issuers and their advisors look closely to such guidance, which therefore has the desired effect of bringing the issue before the corporate decision-makers. The SEC interpretive guidance identifies the existing heads of disclosure of Regulation S-K, under which climate change disclosure may be required if it is "material,"[38] and further identifies four areas—impact of legislation and regulation, international accords, indirect consequences of regulation or business trends, and physical impact of climate change—as examples of situations where climate change disclosure may be required.

The SEC interpretive guidance comes after several years of lobbying from CalPERS, CERES and other institutional investors and civil society groups.[39]

5. Conclusion: The normative picture and the way ahead

As was noted earlier, Indian law provisions on CSR are scattered across legislations in different areas and need to be collated under a single umbrella for corporates to be able to develop a systemic or institutional approach to CSR and their responsibilities to stakeholders. With some additional policy input and legislative changes, the existing corporate governance legal system can provide the enabling environment for improved ESG integration by corporates within their business.

Within the field of board responsibilities towards stakeholders, the scattered provisions on board responsibility towards certain stakeholders, as well as the liability of directors for a company's non-compliance with environmental and labour laws make it clear that Indian law intended for the board to be responsible, at least to certain stakeholders. However what is missing is legal or regulatory guidance regarding a comprehensive approach towards stakeholders, which includes philanthropic initiatives. This has the potential to be addressed under the proposed Stakeholder Relationship Committee under the Companies Bill, if its purpose can be broadened beyond merely addressing stakeholder grievances. Unlike the UK Companies Act (which identifies key stakeholders and requires the board to consider their interests) the proposed change under the Companies Bill leaves the identification of its stakeholders to the board/committee of the concerned corporate. This provision should therefore be utilised by corporates to engage in a strategic stakeholder identification and engagement exercise. Clause 160(1)(e) of the proposed Companies Bill regarding corporate philanthropy also needs to be clarified and the discretionary CSR spending allowed under the Companies Act should also be utilised by boards in a strategic manner.

In the area of CSR reporting, although scattered ESG reporting is mandated under the disclosure regime, a more holistic approach is needed, with regard to corporate practice as well as at the policy level. Among corporates, the trend as to ESG reporting, within Annual Reports and as stand-alone sustainability reports, must spread beyond the large corporates. In view of the limitations of the filings databases maintained by SEBI and the stock exchanges, all corporates should consider making their filings simultaneously available on their websites.

A broad-based policy discussion is also needed regarding the legislative, regulatory and other changes needed for a deeper integration of significant ESG issues into the disclosure regime, by identifying ESG issues that should be brought to the attention of the board, by requiring the board and management to disclose such information in the board report, as was done with energy consumption under Section 217(1)(e) of the Companies Act; ESG data that should be collected, audited and broadly disclosed to stakeholders through the Annual Report; and additional ESG data that is useful for stakeholders, but cumbersome for all corporates to collect and verify, which could be disclosed under a sustainability reporting framework that can be voluntarily adopted by corporates.

In the policy discussion, the examples of other countries can be referred to, although legal policy changes must be carefully considered in light of local conditions (Varottil, 2009).

A combination of drivers is required for improved corporate responsibility, and the law is only one of them. The value of legal change should not be overestimated—India is an example of how the best laws, if not effectively enforced, are powerless to change behaviour. But the power of law should also not be underestimated—as legal developments regarding non-financial reporting in other countries have shown, legal and regulatory changes can highlight issues and create awareness, and thereby catalyse a movement towards corporate responsibility.

References

Asian Corporate Governance Association. (2010). *ACGA White Paper on Corporate Governance in India.*

Association for Stimulating Know How. (2010). “Exploring the business case for CSR in India”. Association for Stimulating Know How. (Working Title, Unpublished Manuscript.)

Business for Social Responsibility. (2008). “Environmental, social and governance:

Moving to mainstream investing?". Accessed on 15 April, 2010 (http://www.bsr.org/reports/BSR_ESG_Mainstream_Investing.pdf).

Carroll, A. B. (1991). "The pyramid of corporate social responsibility: Toward the moral management of organizational stakeholders". *Business Horizons*, 34, pp. 39–48.

Dunfee, T. D. (2008). "Stakeholder theory. Managing corporate social responsibility in a multiple actor context". A. Crane, A. McWilliams, D. Matten, J. Moon, & D. Siegel (Eds.), *Corporate Social Responsibility* (p. 346–363). London: Oxford University Press.

Egan, M. L., F. Mauleon, D. Wolff, & M. Bendick Jr. (2003). "France's nouvelles regulations economiques: Using government mandates for corporate reporting to promote environmentally sustainable economic development". Paper prepared for presentation at the 25th Annual Research Conference of the Association for Public Policy and Management, Washington, DC. Accessed on 13 March, 2010 (http://www.bendickegan.com/pdf/EganMauleonWolffBendick.pdf).

Elkington, J. (1997). Cannibals with forks: *The triple bottom line of 21st century business.* Oxford: Capstone Publishing.

Gautam, R. (2010). "Legal framework for corporate social responsibility. A survey of Indian law". Accessed on 25 May, 2010 (http://alpha.responsible-business.in/Legal-Framework-Survey).

Global Public Policy Institute. (2006). "Trends in non-financial reporting". Paper prepared for the United Nations Environment Programme, Division of Technology, Industry and Economics. Accessed on 13 March, 2010 (http://www.gppi.net/fileadmin/gppi/nonfinancialreporting01.pdf).

Global Reporting Initiative. (2009). "Reaching investors. Communicating value through ESG disclosures". Accessed on 13 March, 2010 (http://www.globalreporting.org/NR/rdonlyres/B2B8C711-4E1D-4858-AC01-8008DCD239B7/2568/ReachingInvestors.pdf)

Justice Chandrachud, Y. V. (Ed.). (2006). *A. Ramaiyya guide to the Companies Act* (16th ed.). Nagpur: Wadhwa & Company.

Karmayog. (2009). *A report on the Karmayog corporate social responsibility ratings 2008 of the 1000 largest Indian companies. Accessed on 4 March,* 2010 (www.karmayog.org/csr2008).

KPMG. (2008). "International survey of corporate responsibility reporting". Accessed on 27 January, 2010 (http://www.kpmg.nl/Docs/Corporate_Site/Publicaties/Corp_responsibility_Survey_2008.pdf).

KPMG-GRI. (2007). *Reporting the business implications of climate change in sustainability reports*. Accessed on 23 January, 2010 (http://www.kpmg.nl/Docs/Corporate_Site/Publicaties/GRI_KPMG_CC_Report.pdf).

Kumar Mangalam Birla Report. (1999). *Report of the Committee Appointed by the SEBI on Corporate Governance under the Chairmanship of Shri Kumar Mangalam Birla.* Accessed on 15 April, 2010 (http://www.sebi.gov.in/commreport/corpgov.html).

Lin, L. (2009). "Corporate social and environmental disclosure in emerging securities markets". *North Carolina Journal of Law and Commercial Regulation*, 35, pp. 1–32.

Melee, D. (2008). "Corporate social responsibility theories". In A. Crane, A. McWilliams, D. Matten, J. Moon, & D. Siegel (Eds.), Corporate Social Responsibility (p. 47–83). London: Oxford University Press.

Partners in Change. (2007). 4th report on corporate responsibility in India (2006-2007). New Delhi: Partners in Change.

Securities and Exchange Commission. (2010). "Commission guidance regarding disclosure related to climate change". Release Nos. 33-9106; 34-61469; FR-82, dated 8 February 2010. Accessed on 13 March, 2010 (http://www.sec.gov/rules/interp/2010/33-9106.pdf).

Social Investment Forum and Emerging Markets Disclosure Project. (2009). "Corporate sustainability disclosure in emerging markets". Accessed on 26 May, 2010 (http://www.socialinvest.org/projects/iwg/documents/EMDP_UNCTAD_REPORT.pdf).

Sood, A., & B. Arora. (2006). "The political economy of corporate responsibility in India". United National Research Institute for Social Development Programme Paper No. 18. Accessed on 27 February, 2010 (http://www.unrisd.org/80256B3C005BCCF9/search/A00E0FF825FC59AAC1257258002FFC1E?OpenDocument).

Sundar, P. (2000). *Beyond business: From merchant charity to corporate citizenship. Indian business philanthropy through the ages.* New Delhi: Tata McGraw-Hill Publishing Company. Cited in Sood & Arora (2006).

SustainAbility and International Finance Corporation. (2002). *Developing value: The business case for sustainability in emerging markets* (1st ed.). UK: Beacon Press.

SustainAbility and UNEP. (2001). "Buried treasure: Uncovering the business case for corporate sustainability". Accessed on 25 May, 2010 (http://www.sustainability.com/library/buried-treasure).

UNEP, KPMG, GRI, Unit for Corporate Governance in Africa. (2010). "Carrots and sticks: Promoting transparency and sustainability. An update on trends in voluntary and mandatory approaches to sustainability reporting". Accessed on 31 July, 2010 (http://www.globalreporting.org/NR/rdonlyres/08D0C5D6-3B19-4BA2-9F12-540F66F73C5E/4198/Carrrots2010final.pdf).

Varottil, U. (2009). "A cautionary tale of the transplant effect on Indian corporate governance". *National Law School of India Review*, 21(1), pp. 1–49.

Varottil, U. (2010). "A dose of sunlight therapy: Using corporate and securities laws to treat climate change". Accessed on 15 April, 2010 (http://papers.ssrn.com/sol3/papers.cfm?abstract_id=1570346).

Notes

[1] The term corporate has been used intentionally so as not to limit the discussion to entities of a specific legal form, such as companies, but at the same time to clarify that small unorganised businesses are not the focus of this paper (as they face very different governance issues). However where the Companies Act or Listing Agreement provisions are referred to, the use of the term company is appropriate in view of the fact that these laws apply only to companies.

[2] For details, see "PSE Dept may come under corporate affairs ministry", The Economic Times, 25 January 2010.

[3] The term CSR is also sometimes used interchangeably with corporate citizenship, enterprise or business responsibility, and even corporate sustainability.

[4] The current draft of the ISO 26000, and related documents and comments are available at http://isotc.iso.org/livelink/livelink?func=ll&objId=3934883&objAction=browse&sort=name (Accessed on 26 January, 2010). The ISO 26000 identifies the following principles of social responsibility—transparency, accountability, ethical behaviour, respect for stakeholder interests, respect for rule of law, respect for international norms of behaviour, and respect for human rights. It also gives guidance to organisations for the integration of social responsibility within the organisation.

[5] The Ruggie framework (2008) is available at http://www.reports-and-materials.org/Ruggie-report-7-Apr-2008.pdf (Accessed on 26 January, 2010). The framework comprises three core principles—the State duty to protect against human rights abuses by third parties, including business; the corporate responsibility to respect human rights; and the need for more effective access to remedies (by the State—judicial and non-judicial—as well as by company-level remedies).

[6] Gautam (2010) makes a case for the inclusion of legal compliance within the definition of CSR. There is some academic support for this contention, like Carroll's CSR pyramid (Carroll, 1991) which includes legal responsibilities as one of the levels of corporate responsibility. Compliance with laws is also one of the principles underlying

the ISO 26000 Social Responsibility Standard, although its inclusion proved somewhat contentious in the ISO negotiations.

[7] A survey of 500 companies operating in India shows that about 70% support weaker sections of society through their community development initiatives (Partners in Change, 2007). These initiatives target (in descending order of popularity among the survey universe) people affected by natural disasters, children, women, youth, the girl child, physically challenged, elderly, people living with diseases, tribal, homeless, and dalit. Significant issues include health and education. In terms of manner of engagement, the survey noted (again, in descending order of popularity) employee volunteering, cash donations, donation of products and services, provision of company facilities, skills/business training to NGO staff and preferential purchase of materials from community or NGO staff. Another significant regular CSR survey in India notes that 11% of the 1000 surveyed companies do CSR through their own foundation or trust and key areas for initiatives include education, healthcare and rural development (Karmayog, 2009, p. 9).

[8] The transcript of the speech is available at http://pmindia.nic.in/speech/content.asp?id=548 (Accessed on 21 January, 2010).

[9] For a succinct summary and assessment of Friedman's theory, see Melee (2008, pp. 55–62).

[10] One of the barriers to the integration of environmental, social and governance (ESG) concerns into mainstream investing is the short-term focus of many investors and the importance of earning targets over long-term economic value (Business for Social Responsibility, 2008).

[11] For instance the corporate governance field of "risk management" can benefit from the integration of CSR or environmental and social risks, which will give investors a more holistic picture. Similarly elements of CSR or environmental and social audit can be included within the financial audit function.

[12] For instance should the role of the board be strategic guidance, management, oversight, watchdog function, or a combination of the above? Although the law is silent on the subject, there has been some discussion on this in academic literature. Further the board charters of some companies specifically address this issue by setting forth the role of the board as well as of each committee. The Kumar Mangalam Birla Report (1999) identified the role of the board as: directing the company (i.e. formulating policies and plans), control of the company and management, and accountability to shareholders.

[13] For instance, Section 25 of the Contract Labour (Regulation and Abolition) Act, 1970, Section 11 of the Equal Remuneration Act, 1976, and Section 16 of the Environment (Protection) Act, 1986. Gautam (2010) surveys the legal obligations of a business that form the baseline for its corporate responsibility towards stakeholders in the following seven areas of the law—corporate governance, environment, labour, competition, consumer protection, resettlement and rehabilitation and corruption.

[14] See National Small Industries Corp. Ltd. vs. Harmeet Singh Paintal & Ors., Criminal Appeal No. 320-336 of 2010 (Supreme Court), interpreting a similarly worded provision in the criminal law context of directors' liability under Section 141 of the Negotiable Instruments Act, 1881 for bounced cheques.

[15] See U.P. Pollution Board v. Modi Distillery, 1987, 2 Comp LJ 298 (SC). However, the Chairman and Vice Chairman were held to not be responsible for the conduct of the company's business under a similar provision in the Air (Prevention and Control of Pollution) Act, 1981 in N. A. Palkhiwala v. M. P. Pradhushan Niwaran Mandal, Bhopal, 1990 Cr. LJ 1856 (MP).

[16] See Siddharth Kejriwal v. ESI Corp., (1997) 90 Com Cases 496 (Kar.), in the context of the Employee State Insurance Act; Rajagopalachari (S.) v. Bellary Spg. And Wvg. Co. Ltd., (1997) Com Cas 485 (Kar.) in the context of the Employee Provident Fund Act; and Hari Charan Singh Dugal v. State of Bihar, (1990) 3 Corp LA 234 (Pat), in the context of the Minimum Wages Act.

[17] Section 293(1)(e) of the Companies Act, 1956.

[18] The example cited in Justice Chandrachud (2006) is the donation of a parcel of land to build a road, by which the company itself or its employees are likely to receive some benefits such as improved efficiency or inducement to increased efforts on the part of employees.

[19] Under Section 172 of the UK Companies Act (2006), a director of a company must act in the way he/she considers (in good faith) would be most likely to promote the success of the company including to have regard to "(a) the likely consequences of any decision in the long term, (b) the interests of the company's employees, (c) the need to foster the company's business relationships with suppliers, customers and others, (d) the impact of the company's operations on the community and the environment, (e) the desirability of the company maintaining a reputation for high standards of business conduct".

[20] Clause 158(12) of the Companies Bill (2009).

[21] A model under the stakeholder theory developed to measure the salience of stakeholders and allocate discretionary CSR spending has been proposed in Dunfee (2008).

[22] Although detailed information is required to be disclosed to potential purchasers at an initial public offering, this disclosure to the primary markets is a one-time activity, and therefore closer to the field of investor protection than corporate governance. In this article therefore, we limit the discussion to periodic disclosure.

[23] Several ESG risks and opportunities have been identified that are key to investors and should therefore be disclosed, including "...major public issues...which are linked to key products (e.g., concern over obesity trends affecting companies that sell food products);...issues that will drive changes in company cost structure (e.g., compliance with new legislation, outsourcing and workforce restructuring), and issues that relate to reputation" (Global Reporting Initiative, 2009, p. 7). The recent British Petroleum oil spill off the Gulf of Mexico is a classic example of an environmental risk and potentially enormous environmental liability which resulted in the plummeting of the company's share price.

[24] Items 101(c)(xii) and 103 of Regulation S-K read with Item 1 (Business) of Form 10-K. See, especially, Instruction 5 to Item 103 of Regulation S-K read with Item 3 of Form 10-K which requires even routine environmental litigation to be disclosed subject to certain conditions. Other routine legal proceedings need not be disclosed.

[25] Around 56 Indian companies report on environmental and social factors; 35 of these produce sustainability reports using the reporting guidelines of the Global Reporting Initiative, according to UNEP, KPMG, GRI, Unit for Corporate Governance in Africa (2010).

[26] A study which ranked 10 emerging markets based on the reporting of identified ESG indicators in their annual reports by 10 economically significant companies in each of these countries, placed India in the eighth position, followed only by China and Israel (Social Investment Forum and Emerging Markets Disclosure Project, 2009). See also the studies cited in footnotes 75 and 76 in Varottil (2010).

[27] Unlike the EDGAR database in which all public filings of US public companies are maintained and accessible by the public, the two Indian databases—EDIFAR and Corpfilings—are difficult to access. Further, not all listed companies' information is maintained in these databases (Asian Corporate Governance Association, 2010, pp. 39–40).

[28] Since ESG reporting holds the key to reducing a corporate's environmental and social footprint, is the focus of the following section will be ESG reporting rather than reporting on the corporate's philanthropic initiatives.

[29] Global Reporting Initiative Reporting Guidelines (p. 3), Accessed on 23 January, 2010 (www.globalreporting.org).

[30] Available at http://www.globalreporting.org/ReportingFramework ReportingFramework Downloads (Accessed on 23 January, 2010). A 2008 study by KPMG found that of the Global Fortune 250 companies, nearly 80% issued corporate responsibility reports, and another 4% integrated some aspects of corporate responsibility into their annual reports. Of the G250 companies, 77% used the GRI G3 Reporting Guidelines to do so (KPMG, 2008).

[31] A 2007 KPMG and GRI study on climate change found that "companies reported far more on potential opportunities than financial risks for their companies from climate change" (KPMG-GRI, 2007).

[32] Rule 10b-5 of the Securities Exchange Rules under US law and regulatory guidance under this rule provide a detailed frame of liability for false and misleading statements made to the public. Under common law, Hedley Byrne & Co. Ltd. v. Heller and Partners Ltd., (1963) All ER 575 (House of Lords) establishes the liability of directors towards shareholders who rely on a misstatement.

[33] A model for understanding the complementarity of mandatory and voluntary reporting is proposed in Box 1 (p. 8) of UNEP, KPMG, GRI, Unit for Corporate Governance in Africa (2010).

[34] For an overview of ESG disclosure under the securities laws of other countries, see Lin (2009), pp.3–4 regarding developed countries, and pp. 15–25 regarding securities ESG disclosure in five emerging markets (South Africa, Malaysia, China, Taiwan, and Thailand).

[35] Article 116, paragraph 4 of the NRE. For an English summary, see Table 1 in Egan et al., (2003, pp. 11–12).

[36] See Global Public Policy Institute (2006, p. 27).

[37] For details, see Bursa Malaysia (Case Study) on "WFE – World Federation of Exchanges". Accessed on 13 March, 2010 (http://www.world-exchanges.org/sustainability/m-6-4-1.php).

[38] Under the SEC Release, climate change disclosure may be required in the Annual Report on Form 10-K under the headings Business, Legal Proceedings, Risk Factors, and MD&A of Regulation S-K.

[39] For a list of the several petitions submitted to the SEC for interpretive guidance on climate change, see footnote 20 in Securities and Exchange Commission (2010, p. 7).

[40] For details, see National Textile Workers' Union v. P. R. Ramakrishnan, A.I.R. 1983 SC 75. The Companies Act also provides for overriding preferential payment for workmen's dues in case of winding up under Section 529A of the Companies Act, which is currently slated to continue in the same form in the Companies Bill, 2009 as Clause 301 of the current draft.

[41] Annexure IA to Clause 49 of the Listing Agreement.

[42] See Annexure 1C to Clause 49 of the Listing Agreement for details regarding the mandatory items of disclosure, and Annexure 1D for details on the optional disclosure items of corporate governance.